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Jeffrey A. Monhart

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A PRIMER ON THE DEVELOPING DOCTRINE OF CONSTRUCTIVE FRAUD IN MONTANA

Jeffrey A. Monhart*

INTRODUCTION

Inconsistent jurisprudence has clouded the recent history of constructive fraud in Montana. A major problem has ensued from the Montana Supreme Court's reading of a fiduciary duty into the statute addressing constructive fraud. Constructive fraud is the breach of a legal or equitable duty that injures another party. It does not require intent. Constructive fraud encompasses acts, omissions and failures to disclose. The Montana code recognizes a constructive fraud claim consisting of:

- (1) *any breach of duty* which, without an actually fraudulent intent, gains an advantage to the person in fault or anyone claiming under him by misleading another to his prejudice or to the prejudice of anyone claiming under him; or
- (2) any such act or omission as the law especially declares to be fraudulent, without respect to actual fraud.¹

The constructive fraud statute has remained virtually unchanged as a part of Montana law since its enactment in 1895.

As will be noted in Section IV of this comment, although the statute indicates that a low threshold ("any breach of duty") suffices for a constructive fraud claim, the Montana Supreme Court has at times insisted that only the breach of a fiduciary duty that gains an advantage to the person in fault is actionable.² This approach harmonizes with the analysis of the Field Code Commissioners, who considered situations of trust in formulating the constructive fraud statute upon which the Montana statute is based.³

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1. MONT. CODE ANN. § 28-2-406 (1989)(emphasis added).

2. See *infra* Section IV.

3. See *Conkey v. Bond*, 34 Barb. 276, 287 (1861) ("the courts exercise a most jealous scrutiny" to "all employments of a fiduciary character"). The Montana constructive fraud statute derives from California Civil Code §1573 and Field Code §758. The California constructive fraud statute is virtually identical to its Montana counterpart. California courts also vacillate on the fiduciary duty requirement. See, e.g., *Carter v. Seaboard Fin. Co.*, 33 Cal. 2d 564, 203 P.2d 758 (1949) (Seller's failure to inform buyer that a truck had been in a wreck did not constitute constructive fraud because the buyer and seller were not in a fiduciary relationship.); *Glickman v. New York Life Ins. Co.*, 16 Cal. 2d 626, 107 P.2d 252 (1940) (False representations by insurer's agent to insured, resulting in an improper release of right, amounted to constructive fraud.). The economic and social differences between nine-

Moreover, constructive fraud may be easier to prove where an established fiduciary relationship exists.⁴ Because constructive fraud removes the scienter requirement, the court may have erected the fiduciary duty requirement as a barrier to marginal claims that would have perished under the more stringent requirements of actual fraud. In effect, the court may have substituted the fiduciary duty requirement for scienter. The court may, however, have forecasted a flood of claims that never in fact materialized.

Clearly, the plaintiff must prove (1) the existence of a duty, or (2) an act or omission considered fraudulent by law.⁵ The culpable party also must have gained an advantage over the plaintiff or one claiming under the plaintiff. Notably absent from the statute is the requirement of a fiduciary duty. Nonetheless, the court has determined that, unless special circumstances prevail, "duty" means (1) fiduciary duty, or (2) duty to disclose. As a result, Montana has two lines of recent cases that conflict. The Montana Supreme Court has not expressly overruled any of the cases discussed in this comment, thus, the practitioner must carefully compare his or her fact pattern to these recent cases to predict the judicial resolution.

Regrettably, the court's constructive fraud jurisprudence has been inconsistent. One line of cases in the past decade has indicated that a fiduciary relationship between the litigants is essential to the claim ("the *Morse* cases").⁶ Another line of cases ("the *Mends* cases")⁷ suggests that a fiduciary relationship is not vital,

teenth-century New York and California and contemporary Montana are obvious, thus the reasoning for applying an antiquated fiduciary duty requirement in Montana has less force. Some Montana constructive fraud claims, for example, involve arms-length transactions. A literal reading of the Montana constructive fraud statute would preserve breaches of fiduciary duty but encompass legitimate claims for other breaches of legal or equitable duty.

4. 37 C.J.S. *Fraud* §2 (1943).

5. *Wiberg v. 17 Bar, Inc.*, 241 Mont. 490, 788 P.2d 292 (1990). See also *Fleming v. Fleming Farms, Inc.*, 221 Mont. 237, 717 P.2d 1103 (1986) (a constructive fraud claim failed for lack of an established duty). Typically, the "act" is an affirmative misrepresentation; the "omission" is the failure to speak when there is a duty to speak.

6. *Morse v. Espeland*, 215 Mont. 148, 696 P.2d 428 (1985). See also *Coles Dep't Store v. First Bank (N.A.)-Billings*, 240 Mont. 226, 783 P.2d 932 (1989); *Bottrell v. American Bank*, 237 Mont. 1, 773 P.2d 694 (1989); *Pipinich v. Battershell*, 232 Mont. 507, 759 P.2d 148 (1988); *Rowland v. Klies*, 223 Mont. 360, 726 P.2d 310 (1986); *Ryckman v. Wildwood, Inc.*, 197 Mont. 154, 641 P.2d 467 (1982); *Local Union No. 400 v. Bosh*, 220 Mont. 304, 715 P.2d 36 (1986); *Purcell v. Automatic Gas Distrib.*, 207 Mont. 223, 673 P.2d 1246 (1983); *Deist v. Wachholz*, 208 Mont. 207, 678 P.2d 188 (1984).

7. *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981). See also *Hobbs v. Pacific Hide & Fur Depot*, 236 Mont. 503, 771 P.2d 125 (1989); *First Bank (N.A.)-Billings v. Clark*, 236 Mont. 195, 771 P.2d 84 (1989); *Drilcon, Inc. v. Roil Energy Corp.*, 230 Mont. 166, 749 P.2d 1058 (1988); *McJunkin v. Kaufman & Broad Home Sys., Inc.*, 229 Mont. 432, 748 P.2d 910 (1987); *McGregor v. Mommer*, 220 Mont. 98, 714 P.2d 536 (1986); *Poulsen v. Treasure State Indus., Inc.*, 192 Mont. 69, 626 P.2d 822 (1981); *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155 (1980). A recent opinion muddies the water further by focusing on a duty to

but that "special circumstances" militate for a finding of constructive fraud. Still another series of opinions does not address the fiduciary relationship issue in a constructive fraud context.⁸ The court awaits the model fact pattern that will enable it to squarely address the fiduciary relationship issue.⁹ Perhaps given the diverse facts that appear before the Montana court, such a definitive answer is ill-advised.

Regardless of the sources of the confusion, however, the Montana bar needs an overview of recent constructive fraud precedent as a guide for litigation, counselling and negotiation. The doctrine has evolved rapidly in Montana but no scholarly work to date has squarely addressed the constructive fraud statute.¹⁰ This article will focus on a working definition of constructive fraud, with reference to the *Morse* and *Mends* cases and their progeny. The article will next acquaint the reader with the current state of the law on constructive fraud and recommend a faithful construction of the statute. This effort will require emphasis on fiduciary relationships and special circumstances. Finally, the article will suggest how to avoid incurring liability during the negotiation stage and will comment on litigating the constructive fraud claim.

I. DEFINITION OF CONSTRUCTIVE FRAUD

The policy underlying constructive fraud is that the wrongdoer, regardless of actual dishonesty or intent, should not benefit from his or her own wrong. Constructive fraud falls under Title 28 of the Montana Code Annotated, pertaining to contracts and other obligations. Fundamentally, contracts must be formed by free consent.¹¹ The constructive fraud claim exists, in part, to provide redress to parties injured by the fraudulent formation of contracts. The claim is thus used to rescind fraudulently procured contracts.

Constructive fraud relieves the plaintiff of the burden of prov-

disclose. *Amundson v. Wortman*, 238 Mont. 207, 777 P.2d 315 (1989).

8. *Kitchen Krafters, Inc. v. Eastside Bank*, 242 Mont. 155, 789 P.2d 567 (1990); *Zugg v. Ramage*, 239 Mont. 292, 779 P.2d 913 (1989); *Larsen v. Opie*, 237 Mont. 108, 771 P.2d 977 (1989); *Albers v. Bar ZF Ranch, Inc.*, 229 Mont. 396, 747 P.2d 1347 (1988); *Fleming v. Fleming Farms, Inc.*, 221 Mont. 237, 717 P.2d 1103 (1986); *Nelson v. Davis Modern Mach.*, 220 Mont. 347, 715 P.2d 1052 (1986).

9. Numerous justices have stirred up this maelstrom. Justices Barz, Daly, Weber, Turnage, Sheehy, Shea, McDonough, Gulbrandson, Hunt, Morrison and District Judge Henry Loble all have written opinions in the past decade addressing constructive fraud.

10. *But see* Comment, *Hidden-But-Discoverable Defects: Resolving The Conflicts Between Real Estate Buyers and Brokers*, 50 MONT. L. REV. 331 (1989) (authored by K. Culum).

11. MONT. CODE ANN. § 28-2-102 (1989). Despite the "breach of duty" language, constructive fraud is a contract cause of action. It is not a tort.

ing "intent to deceive" or "dishonesty of purpose."¹² In Montana, proof of actual fraud requires a formidable list of elements.¹³ By relieving the injured party of this burden, the law guards public or private confidences, as well as public interests.¹⁴ Constructive fraud, by removing the scienter requirement of actual fraud, also enables a plaintiff to pursue a claim that otherwise would not be viable. Implicitly, the constructive fraud doctrine also encourages candor and good faith conduct in relationships (whether commercial or familial) founded on trust.

As noted, the court has read a fiduciary duty requirement into the constructive fraud statute. Currently, constructive fraud arises from breach of a fiduciary duty,¹⁵ or a duty to disclose in certain special circumstances.¹⁶ The constructive fraud claim arises from certain relationships, such as attorney-client,¹⁷ debtor-creditor,¹⁸ vendor-vendee,¹⁹ employer-employee,²⁰ and broker-investor,²¹ among others.²² Constructive fraud usually accompanies other claims such as breach of contract, breach of the covenant of good faith and fair dealing, actual fraud, negligent misrepresentation, and breach of warranty. It may also be raised as an affirmative

12. *Batten v. Watts Cycle & Marine, Inc.*, 240 Mont. 113, 117, 783 P.2d 378, 381 (1989), cert. denied, 110A S. Ct. 1826 (1990).

13. *Lee v. Stockmen's Nat'l Bank*, 63 Mont. 262, 284, 207 P. 623, 630 (1922). A prima facie case of actual fraud consists of:

(1) [a] representation; (2) its falsity; (3) its materiality; (4) the speaker's knowledge of its falsity, or ignorance of its truth; (5) his intent that it should be acted upon by the person and in the manner reasonably contemplated; (6) the hearer's ignorance of its falsity; (7) his reliance upon its truth; (8) his right to rely thereon; (9) and his consequent and proximate injury.

Id.

14. 37 C.J.S. *Fraud* § 2 (1943).

15. Although the term is quite broad, a fiduciary duty generally arises where one party reposes trust or confidence in another. The fiduciary may exercise superiority or influence over the party reposing the trust or confidence. 37 AM. JUR. 2d *Fraud and Deceit* § 16 (1968).

16. The special circumstances seem to be unique to particular cases, which frustrates their application by analogy (at least since the doctrine came into its own a decade ago). As the body of law develops, a more diverse array of fact patterns may afford the practitioner more options.

17. *Morse v. Espeland*, 215 Mont. 148, 696 P.2d 428 (1985).

18. *Deist v. Wachholz*, 208 Mont. 207, 678 P.2d 188 (1984).

19. In the vendor-vendee context, constructive fraud arises from arm's-length transactions. *E.g.*, *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155 (1980). Part VI, *infra*, addresses counselling and negotiation.

20. *Hobbs v. Pacific Hide & Fur Depot*, 236 Mont. 503, 771 P.2d 125 (1989).

21. *Larsen v. Opie*, 237 Mont. 108, 771 P.2d 977 (1989).

22. Other examples of fiduciary relationships include "husband and wife, . . . partners, . . . principal and agent, . . . guardian and ward, . . . physician and patient." 34 CAL. JUR. 3d *Fraud and Deceit* § 27 (1977).

defense.²³ A successful constructive fraud claim may result in rescission of a contract.²⁴ Generally, the court has relied on its own constructive fraud jurisprudence and has rarely borrowed authority from other jurisdictions.

The foregoing definition rests on the horns of the fiduciary duty dilemma, however. To arrive at the state of the current Montana law on constructive fraud, it is first necessary to examine the *Mends* cases and their rivals, the *Morse* cases.

II. THE *MENDS* CASES

A. *The Vendor-Vendee Context*

In *Mends*, the plaintiffs contacted the Dykstras, owners of a Belgrade house, after noticing a "For Sale" sign outside defendants' house.²⁵ Impressed by the appearance of the house and its location, the plaintiffs tendered an earnest-money deposit.²⁶ Plaintiffs visited the house three times in as many months and walked through the house and yard at will.²⁷ During these visits, the defendants pointed out that the house lacked central heating, but had two fireplaces.²⁸ The defendants informed plaintiffs that Mr. Dykstra, a carpenter, built the house and that the Dykstra family lived comfortably there all year long.²⁹ The defendants remarked that the pipes did not freeze, but that parts of the house needed finishing and insulation.³⁰ The defendants answered in the negative when asked if the house had other problems.³¹

The plaintiffs noticed numerous defects made apparent by cooler, rainy weather. A fireplace malfunctioned and filled the house with smoke; another fireplace disintegrated from the heat.³² A chimney leaked water during rains.³³ In repairing the damage, the plaintiffs observed more defects, which a housing inspector confirmed.³⁴ Shoddy, makeshift workmanship became apparent

23. *Amundson v. Wortman*, 238 Mont. 207, 777 P.2d 315 (1989).

24. *Deist v. Wachholz*, 208 Mont. 207, 678 P.2d 188 (1984).

25. *Mends v. Dykstra*, 195 Mont. 440, 441, 637 P.2d 502, 503 (1981).

26. *Id.*

27. The *Mends* cases tend to be fact-laden opinions. The court has scrutinized the records at length—a discipline that favors the merits of the cases rather than distinguishable precedent.

28. *Mends*, 195 Mont. at 441, 637 P.2d at 503.

29. *Id.* at 441-42, 637 P.2d at 503.

30. *Id.* at 442, 637 P.2d at 503.

31. *Id.*

32. *Id.*

33. *Id.* at 442-43, 637 P.2d at 503.

34. *Id.* at 443, 637 P.2d at 503-04.

upon closer inspection. Among the defects were upside-down insulation, exposed wiring, and structural supports balanced or wired together.³⁵ A professional contractor testified that the Dykstra's plumbing had frozen repeatedly in the winter.³⁶ The contractor advised plaintiffs to bulldoze the house and begin anew.³⁷ A Bozeman city building inspector confirmed these defects and revealed other hazards that rendered the structure unhealthy and a fire hazard.³⁸ Plaintiffs' efforts to seek redress from the Dykstras were fruitless.³⁹

The lower court decided that constructive fraud had no place in the trial. It ruled that constructive fraud was not an issue, refused to instruct the jury on constructive fraud,⁴⁰ and told counsel not to mention constructive fraud in closing arguments. Defendants compounded the error by arguing that no fiduciary duty flowed to the Mends because they were "parties to an arm's length transaction," not friends or acquaintances.⁴¹

The *Mends* court accepted the parties' concurrence that breach of duty to disclose material facts is essential to constructive fraud. Justice Weber correctly observed that "there was not a fiduciary relationship or a confidential relationship between the parties, but there may have been special circumstances which in Montana can justify the finding of constructive fraud."⁴² This observation set in motion the conflict between the *Morse* cases and the *Mends* cases.⁴³

The Montana Supreme Court noted, but did not follow, precedent that held that a duty to disclose hinged on a fiduciary relationship between seller and buyer.⁴⁴ Three Montana cases convinced the court, however, that fiduciary duty is not an indispensable element of constructive fraud. *Moschelle v. Hulse*,⁴⁵ the court reckoned, supported a finding that "a pattern of repeated concealments of the true state of affairs concerning the condition

35. *Id.* at 443, 637 P.2d at 504.

36. *Id.*

37. *Id.* at 444, 637 P.2d 504.

38. *Id.*

39. *Id.* at 443, 637 P.2d at 504.

40. The plaintiffs' proposed jury instruction was identical to the constructive fraud statute. *Id.* at 446, 637 P.2d at 506.

41. *Id.* at 448, 637 P.2d at 506.

42. *Id.* at 449, 637 P.2d at 507.

43. The *Mends* cases require a breach of fiduciary duty as a prerequisite to constructive fraud. See *supra* note 7 and *infra* Part IV.

44. *Lyle v. Moore*, 183 Mont. 274, 599 P.2d 336 (1979). The plaintiffs argued that *Lyle* also allowed exceptions when the duty to disclose should exist.

45. 190 Mont. 532, 622 P.2d 155 (1980).

of the premises"⁴⁶ constituted constructive fraud.

Moschelle imparted more than this accurate statement, though, and it is worth pausing to reflect on the meaning of Justice Shea's opinion. *Moschelle* offers the proper construction of the constructive fraud statute: "[d]ishonesty of purpose or intent to deceive is not a requirement under [Montana Code Annotated section 28-2-406]."⁴⁷ *Moschelle* involved the defendants' sale to plaintiffs of a Virginia City tavern. The defendants made false representations before the sale regarding the condition of the premises and sufficiency of earnings from the tavern.⁴⁸ In both *Moschelle* and *Mends*, the defendants misrepresented the condition of the sale premises. In both cases, the number and severity of defects were known to the defendants but not revealed to the plaintiffs. The plaintiffs in both cases could ascertain the undisclosed defects only upon concerted effort.⁴⁹ The court in *Moschelle* considered these factors as well as defendants' refusal to provide business records that would not have substantiated their representations of the tavern's earnings.⁵⁰ The *Moschelle* court determined "there can be no doubt that [the defendants'] representations concerning the subject of the sale amounted to constructive fraud. . . . [T]heir statements were misleading on their face and thus required further elaboration so as not to give the plaintiffs the wrong impression."⁵¹ The court added that "[t]he facts indicate a pattern of repeated concealments of the true state of affairs concerning the condition of the premises and probable business earnings. Withholding relevant facts concerning purchased property can be a fraudulent act."⁵² The *Moschelle* court looked beyond its own cases⁵³ in holding that "the defendants were under a duty to make such disclosures as would erase the false impressions created in the minds of the plaintiffs that repairs to the premises were not needed and that

46. *Id.* at 539, 622 P.2d at 159.

47. *Id.* at 537, 622 P.2d at 158.

48. *Id.* at 535-36, 622 P.2d at 157.

49. In *Moschelle*, the plaintiff could learn of a rotted foundation only by crawling under the floor. In *Mends*, the plaintiff learned of serious defects after hiring an inspector, a plumber, and a contractor.

50. *Moschelle*, 190 Mont. at 535, 540, 622 P.2d at 157, 159-60.

51. *Id.* at 538, 622 P.2d at 158. The court made the valuable observation that in negotiating a sale, elaboration is necessary to preclude a constructive fraud allegation. See *infra* Part VI.

52. *Moschelle*, 190 Mont. at 539, 622 P.2d at 159.

53. The court cited authority from Michigan (*Olitkowski v. St. Casimir's Sav. & Loan Ass'n*, 302 Mich. 303, 4 N.W.2d 664 (1942)) and Wyoming (*Twing v. Schott*, 80 Wyo. 100, 338 P.2d 839 (1959)), as well as 37 C.J.S. *Fraud* §2c(1) (1943); 12 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS §1498 (3d ed. 1970); RESTATEMENT OF CONTRACTS §472(1)(b) comment b (1932).

winter earnings were sufficient for the plaintiffs' needs."⁵⁴

The *Mends* court also considered *Poulsen v. Treasure State Industries, Inc.*,⁵⁵ wherein the court ruled that the defendant sellers' failure to disclose to the buyers "serious impairments to the property which [plaintiff buyers] had no reason to suspect"⁵⁶ constituted constructive fraud. In *Poulsen*, the plant manager of the defendant corporation misrepresented to the buyers a shale plant's status with the local Board of Health,⁵⁷ and also failed to disclose a material water drainage problem.⁵⁸ Here again, the court found constructive fraud liability where (1) defendant knew of material defects, and (2) failed to disclose the defects.

The court in *Mends* cited a third case, *Russell v. Russell*,⁵⁹ for the accord that "fraud is complete where a vendor knowingly suppresses a serious vice of his property which the vendee had no reason to suspect."⁶⁰ The *Mends* court held that the district court erroneously refused plaintiffs' constructive fraud jury instruction.⁶¹ It closely examined the facts and concluded that "statements by the [defendants] which, while not strictly untrue, were sufficiently misleading to create a duty to disclose"⁶² and that "constructive fraud was a crucial element, if not the crucial element of this case."⁶³ The presence of a contract and the absence of a special relationship did not deter the court from its finding.⁶⁴

The court cited *Mends* in a recent case involving an arms-length property transaction. The defendants in *McGregor v. Mommer*⁶⁵ contracted with the plaintiffs for the purchase of a gas station and warehouse operation. The defendants provided the plaintiffs a prospectus at their initial meeting.⁶⁶ The defendants had prepared the prospectus for realtors.⁶⁷ The prospectus purported

54. *Moschelle*, 190 Mont. at 539, 622 P.2d at 159.

55. 192 Mont. 69, 626 P.2d 822 (1981).

56. *Id.* at 81, 626 P.2d at 829.

57. *Id.* at 80, 626 P.2d at 829.

58. *Id.* at 73, 626 P.2d at 828-29.

59. 152 Mont. 461, 452 P.2d 77 (1969). In *Russell*, the plaintiffs apparently pleaded simply "fraud" and did not designate either actual or constructive fraud. The court sua sponte concluded that the defendant seller's failure to disclose that a septic system actually was on adjoining property constituted constructive fraud. *Id.* at 465, 452 P.2d at 79.

60. *Id.* at 466, 452 P.2d at 79-80 (quoting *Burkett v. J.A. Thompson & Son*, 150 Cal. App. 2d 523, 310 P.2d 56 (1957)).

61. *Mends v. Dykstra*, 195 Mont. 440, 451-52, 637 P.2d 502, 508-09 (1981).

62. *Id.* at 451-52, 637 P.2d at 508.

63. *Id.* at 452, 637 P.2d at 509.

64. *Id.* at 451, 637 P.2d at 508.

65. 220 Mont. 98, 714 P.2d 536 (1986).

66. *Id.* at 101, 714 P.2d at 538.

67. *Id.*

to list net receipts for the business.⁶⁸ The plaintiffs requested backup information for the prospectus figures and defendants provided a "Financial Statement" that showed the identical numbers, but which did not include operating expenses.⁶⁹ The plaintiffs discovered after the sale that the prospectus figures represented gross income, not net receipts.⁷⁰ The defendants listed customers in the prospectus but failed to disclose that a key customer, accounting for thirty-five percent of their receipts, would not be available after the contract date.⁷¹ The defendants also did not reveal that the plaintiffs would need to take a jobber contract (rather than a consignee contract, which required less operating capital) with its gasoline distributor.⁷² After struggling with cash flow, closing the wholesale operation, and leasing the gas station, the plaintiffs filed a complaint seeking rescission of the contract with defendants and a return of their payments made under the contract.

The court accepted that "the jury had sufficient evidence to find McGregor reasonably relied on the representations."⁷³ The court addressed whether the jury should have been allowed to consider constructive fraud.⁷⁴ The court dismissed the defendants' contention that a fiduciary or confidential relationship is essential to a finding of constructive fraud,⁷⁵ and cited both *Mends* and *Moschelle* in its reasoning.⁷⁶ It held that the lower court properly submitted constructive fraud to the jury. The court also considered that one of the defendants' sons believed McGregor to be unsophisticated in accounting and financial statements.⁷⁷

McGregor represents an affirmation that, in a vendor-vendee context, conveying false impressions, making misleading statements and failing to disclose material facts may lead to a finding of constructive fraud. The case emphasizes that, in this context, no fiduciary or confidential relationship need exist to support such a finding.

The court turned to a consumer transaction in *McJunkin v. Kaufman & Broad Home Systems, Inc.*⁷⁸ One of the issues before

68. *Id.*

69. *Id.* at 101, 714 P.2d at 538.

70. *Id.* at 103, 714 P.2d at 539.

71. *Id.* at 102, 714 P.2d at 538.

72. *Id.* at 102, 714 P.2d at 539.

73. *Id.* at 105, 714 P.2d at 541.

74. *Id.* at 109, 714 P.2d at 543.

75. *Id.* The court correctly adhered to the constructive fraud statute, and was not misled by the *Morse* cases.

76. *Id.*

77. *Id.* at 101, 714 P.2d at 538.

78. 229 Mont. 432, 748 P.2d 910 (1987).

the court was whether the district court properly granted a directed verdict dismissing the plaintiff's claim of constructive fraud. The plaintiff purchased a mobile home from defendant Ponderosa Homes.⁷⁹ McJunkin was dissatisfied with the mobile home after inspecting it and refused to accept the mobile home.⁸⁰ Ponderosa's salesman responded that because the structure was a special order the plaintiff had to take it.⁸¹ The salesman also assured the plaintiff that Ponderosa would take care of everything.⁸² The plaintiff, after moving in, discovered many defects but found little relief from the vendor.⁸³

The plaintiff claimed the district court wrongly found that fiduciary duty is essential to constructive fraud. The supreme court agreed with the plaintiff but found the error harmless. The court observed, "the statute does not require that the plaintiff demonstrate a fiduciary relationship. It merely requires the establishment of a duty. We have recognized that a sufficient duty can arise in a commercial transaction"⁸⁴

McJunkin marks the progress of the line of cases that hold or suggest that a fiduciary relationship is not vital to a constructive fraud claim. By this point in that progress, the court was as emphatic in rejecting that requirement as the *Morse* court was in insisting on its presence. No reference to "special circumstances" appears in *McJunkin*. The court characterized the duty in *McJunkin* as the "duty to refrain from intentionally or negligently creating a false impression by words or conduct."⁸⁵ Evidently, the *McJunkin* court regarded this particular duty as the analogue for "special circumstances."

B. The Services Context

The court left the vendor-vendee relationship behind in deciding *Drilcon, Inc. v. Roil Energy Corp.*⁸⁶ In *Drilcon*, the plaintiff, an oil drilling operation, contracted with the president of Roil to drill an oil well at \$6500 per day on land Roil had secured under a "farm-out" agreement.⁸⁷ Drilcon was to be paid out of an escrow

79. *Id.* at 435, 748 P.2d at 912.

80. *Id.*

81. *Id.*

82. *Id.*

83. *Id.* at 436, 748 P.2d at 912-13.

84. *Id.* at 439-40, 748 P.2d at 915 (citing *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981); *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155 (1980)).

85. *Id.* at 440, 748 P.2d at 915.

86. 230 Mont. 166, 749 P.2d 1058 (1988).

87. Under the farm-out agreement between Roil and Pennzoil, Roil would drill an oil

account set up by a third party; Drilcon had requested the escrow account because Drilcon was unfamiliar with Roil.⁸⁸ The first escrow agent dropped out, so Roil's purported vice-president (Holms) found Sun Escrow to step in.⁸⁹ Both Holms and a Sun officer told Drilcon that the escrow had been funded to cover Drilcon's drilling expenses.⁹⁰

Sun did not pay Drilcon after the latter sent invoices as prescribed so Drilcon asked Holms about the delay. Holms replied that he was unaware of the situation but said he would investigate. Drilcon later learned that Sun could not pay because there was no money in the escrow account.⁹¹ Drilcon again called Holms who said he would look into the situation.⁹² Drilcon quit drilling after two days of no response from Holms and expenses of \$204,000.⁹³ Holms next searched for investors and represented to Drilcon that funding was forthcoming.⁹⁴ Drilcon asked for a written guarantee and a promissory note from Holms before it resumed operations.⁹⁵ Holms sent Drilcon a telegram with a personal guarantee on behalf of himself and White, another Roil officer (White later told Drilcon that the guarantee was unauthorized).⁹⁶ Holms had given Drilcon a bogus security interest in properties and a sham financial statement attesting to his net worth—Holms had no interest in the properties and had a negative net worth.⁹⁷ Moreover, Holms was not a vice-president of Roil.⁹⁸ In reliance on Holms' guarantee and representations, Drilcon fulfilled its obligation.⁹⁹ White knew at that time that the escrow was not funded, that Holms' guarantee was worthless, and that White could not cover the costs himself.¹⁰⁰ Drilcon testified that it believed Roil and its outside investors would pay for the drilling or that White or Holms would pay.¹⁰¹

The issue on appeal was whether a fiduciary relationship is a

well on Pennzoil's leasehold at Roil's risk and expense in exchange for a royalty. *Id.* at 169, 749 P.2d at 1059.

88. *Id.* The jury found Roil was "utilized as a subterfuge to defeat public convenience." *Id.* at 175, 749 P.2d at 1063.

89. *Id.* at 169, 749 P.2d at 1060.

90. *Id.*

91. *Id.*

92. *Id.*

93. *Id.*

94. *Id.* at 170, 749 P.2d at 1060.

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

prerequisite to a finding of constructive fraud. The court collected the Montana cases holding that fiduciary duty is essential and the cases indicating the contrary. The court examined the lower court's constructive fraud instruction that read, in part: "Where a party, by his words or conduct creates a false impression concerning serious impairments or other important matters and subsequently fails to disclose relevant factors, constructive fraud may be found."¹⁰² Significantly, the court found this instruction embodied the elusive "special circumstances" essential to support a jury verdict.¹⁰³

The court held that a fiduciary relationship was unnecessary for a finding of constructive fraud under these "special circumstances"¹⁰⁴ and that substantial credible evidence existed that White committed constructive fraud.¹⁰⁵ *Drilcon* is a significant case because, unlike its predecessors in the *Mends* line of cases, it addresses sophisticated business parties outside of the vendor-vendee context. *Drilcon* shares a similar focus, however, on failure to disclose material facts and on the communication of false impressions to a party acting in reliance on promises. As such, it furthers the advancement of the constructive fraud doctrine. *Drilcon* is especially valuable because it provides examples of "special circumstances." The special circumstances appear to be limited to the facts in *Drilcon*.¹⁰⁶

C. The Banking Context

More recently, in *Simmons v. Jenkins*,¹⁰⁷ the court expressly

102. *Id.* at 171, 749 P.2d at 1061.

103. *Id.* at 172, 749 P.2d at 1061.

104. Among the special circumstances were the use of an improper corporate entity as a shield from personal liability, White's failure to disclose the flaws to creditors, White's failure to assert the truth about Holms' finances when White knew of Drilcon's reliance, and White's failure to inform Drilcon of Holms' lack of corporate office. *Id.* at 170-73, 749 P.2d at 1060-62.

105. *Id.* at 178-79, 749 P.2d at 1065. The district court's instruction accurately paraphrased MONT. CODE ANN. § 28-2-406(1) and declared, "There need be no fiduciary duty or confidential relationship between parties to justify a finding of constructive fraud." *Id.* at 171, 749 P.2d at 1061.

106. Justice Sheehy admonished in his dissent, "We make fuzzy the liability theory of constructive fraud when we go outside the confidential or fiduciary relationships and find that 'special circumstances' can give rise to liability under the theory of constructive fraud." *Id.* at 181, 749 P.2d at 1067 (Sheehy, J., dissenting). Justice Sheehy urged that constructive fraud should be limited to cases involving a breach of duty that arises typically through a confidential or fiduciary relationship. *Id.* One month before, in *McJunkin v. Kaufman & Broad Home Systems, Inc.*, 229 Mont. 432, 748 P.2d 910 (1987), the court had held no fiduciary relationship was necessary.

107. 230 Mont. 429, 750 P.2d 1067 (1988).

followed *McJunkin*.¹⁰⁸ In *Simmons*, the purchasers and appellants (Simmons) named the local bank and the seller's mortgagee as defendants in a constructive fraud claim. Simmons alleged the seller misrepresented a ranch sold under a contract for deed.¹⁰⁹ Simmons claimed that the bank and the mortgagee were liable for constructive fraud and alleged the bank breached a fiduciary duty or duty of good faith.¹¹⁰ The vendee claimed the bank was aware of the sale, had told the vendors to sell, had suggested terms of the sale, and had induced vendees to buy because of seller's loan commitment to the bank.¹¹¹

A bank-customer relationship does not ordinarily create a fiduciary duty except where the bank acts as a financial advisor, not simply as a creditor.¹¹² The debtor must have "a long history of dealing with the bank and evidence of the bank acting as financial advisor in some past capacity."¹¹³ The court found a "tenuous" connection between the vendee and the bank because of a lack of history of dealings, lack of reliance, and lack of advice.¹¹⁴ The mere knowledge by the bank of Simmons' negotiations did not create a fiduciary relationship.¹¹⁵ Moreover, the inference that the bank induced the sale to its benefit by taking advantage of its co-defendants' misrepresentation was also too tenuous.¹¹⁶ In *Simmons*, the court correctly followed the elements of the statute and found no actionable act or omission and no breach of duty.

D. Summary of the *Mends* Cases

Mends impresses one with its patient, careful recitation of the facts, its reasoning and its scrutiny of the authorities. In this regard it contrasts with *Morse v. Espeland*. Most following cases share the careful analysis of *Mends* and its willingness to locate a duty to disclose outside the fiduciary duty ambit. In particular, the cases that follow *Mends* express a willingness to find liability in

108. See *supra* text accompanying note 78 for a discussion of *McJunkin*, which held that the statute did not require that a plaintiff prove a fiduciary relationship.

109. *Simmons*, 230 Mont. at 432, 750 P.2d at 1069. Hall & Hall, a local mortgage bank, appraised most of the vendor's property and estimated the carrying capacity for the acreage including that sold to Simmons. *Id.* at 431, 750 P.2d at 1069.

110. *Id.* at 432-33, 750 P.2d at 1070.

111. *Id.* at 433, 750 P.2d at 1070.

112. *Id.* The court cited *Deist v. Wachholz*, 208 Mont. 207, 678 P.2d 188 (1984), discussed at text accompanying *infra* note 128. See also Bahls, *Termination of Credit for the Farm or Ranch: Theories of Lender Liability*, 48 MONT. L. REV. 213, 236-39 (1987).

113. *Simmons*, 230 Mont. at 433, 750 P.2d at 1070.

114. *Id.*

115. *Id.* at 435, 750 P.2d at 1071.

116. *Id.*

relationships besides that between vendors and vendees.¹¹⁷

In summary, the *Mends* cases involved both major commercial and consumer contracts. Common to each case is the breach of a duty to disclose material information. This breach of duty gained an advantage to the party in breach of the duty to disclose. Thus, these cases adhere to the elements of the statute. In each case, the court looked closely at the type of concealed information and how it adversely affected the plaintiff. In *Mends*, for example, the defendants' failure to disclose material building defects resulted in the plaintiffs paying an inflated price for a seriously flawed property. In *Drilcon*, the court considered that the plaintiff proceeded to fulfill its obligation despite the misrepresentation that it would be paid on time. Unburdened by a narrow requirement of fiduciary duty, the court provided relief to these plaintiffs injured by misleading representations or omissions.

III. THE MORSE CASES

The fiduciary duty welter originates in the emphatic, unqualified statement, "[i]f there is no fiduciary duty in the first place, constructive fraud will not lie."¹¹⁸ *Morse v. Espeland*¹¹⁹ flatly contradicted *Mends* without distinguishing the case or even mentioning it. In a fourteen-paragraph opinion, Justice Morrison addressed a suit by an attorney against his client to recover fees from a dissolution proceeding. The client's judgment amounted to \$667,555.75.¹²⁰ The parties had not formally agreed on a fee arrangement, but the client testified she believed from her lawyer's representations that the dissolution would cost \$5000.¹²¹ The client paid the only bill sent to her for her attorney's services, in the amount of \$2,015.98.¹²² After the sizable judgment, the attorney asked for more money. He remarked, "I wouldn't dig ditches for that" when the client reminded him of the \$5000 figure.¹²³ The attorney sued for fees, expenses, costs, and interest and the client counterclaimed for breach of fiduciary duty, actual fraud, deceit, legal malpractice, and constructive fraud. The client appealed the

117. *Mends, Moschelle, Poulsen, and Russell* all involved the vendor-vendee relationship. *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981); *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155 (1980); *Poulsen v. Treasure State Indus., Inc.*, 192 Mont. 69, 626 P.2d 822 (1981); *Russell v. Russell*, 152 Mont. 461, 452 P.2d 77 (1969).

118. *Morse v. Espeland*, 215 Mont. 148, 151, 696 P.2d 428, 430 (1985).

119. 215 Mont. 148, 696 P.2d 428 (1985).

120. *Id.* at 150, 696 P.2d at 429.

121. *Id.*

122. *Id.*

123. *Id.*

lower court's grant of the lawyer's motion for summary judgment on the counterclaim.

The court observed that "[u]nquestionably, an attorney has a fiduciary relationship with a client on most matters" ¹²⁴ and noted that "[c]onstructive fraud is a breach of fiduciary duty." ¹²⁵ Having uttered this momentous pronouncement, the court then undercut it by opining that fiduciary duty rules do not apply to negotiation of a fee because then "an attorney must necessarily deal at arms length with a client." ¹²⁶ The court simply posited, without analysis or citation to the record, that this indeed happened. The court found liability under breach of the covenant of good faith and fair dealing. ¹²⁷

Morse is significant because it reads a fiduciary duty into the constructive fraud statute. *Morse* is also influential because it unequivocally requires a fiduciary duty. Despite its brevity and lack of thorough analysis, *Morse* gained considerable stature because later courts cited its unambiguous holding.

One year earlier, District Judge Henry Loble, sitting for Justice Morrison, authored *Deist v. Wachholz*. ¹²⁸ In *Deist*, the seller of a ranch sued for rescission of a sale contract. ¹²⁹ The seller, a rancher's widow, asked defendant, the vice-president of marketing at a local bank, to locate a buyer after the bank president recommended that the widow sell. ¹³⁰ The widow was a novice to real estate transactions. The defendant did not appear to be an advisor, nor did he negotiate the ensuing sale of the widow's ranch. ¹³¹ He referred an investor to the plaintiff, after negotiations with a first buyer failed. The defendant told the plaintiff that the investor was reputable and that the sale would be a "good deal." ¹³² On the same day she signed the contract for deed, the widow learned that the defendant was one of two investors in the deal, and that the two investors were partners in other local real estate transactions. ¹³³

124. *Id.* at 151, 696 P.2d at 430.

125. *Id.*

126. *Id.*

127. The court unpersuasively analogized the *Morse* attorney-client relationship to *Gates v. Life of Montana Insurance Co.*, 205 Mont. 304, 668 P.2d 213 (1983) and *Dare v. Montana Petroleum Marketing Co.*, 212 Mont. 274, 687 P.2d 1015 (1984). *Morse*, 215 Mont. at 152, 696 P.2d at 431. The *Gates* and *Dare* cases, however, involved employer-employee relationships.

128. 208 Mont. 207, 678 P.2d 188 (1984).

129. *Id.* at 214, 678 P.2d at 192.

130. *Id.* at 212, 678 P.2d at 190-91.

131. *Id.* at 212, 678 P.2d at 191.

132. *Id.* at 213, 678 P.2d at 191.

133. *Id.* at 212-14, 678 P.2d at 191-92.

The district court ruled that the vice-president shared a fiduciary relationship with the plaintiff and that he owed the widow a fiduciary duty as a bank officer and as an agent in the sale.¹³⁴ The supreme court affirmed the finding of fiduciary duty and ruled that such a finding is essential to a constructive fraud claim.¹³⁵ The court recited Montana law holding that usually a bank and its customer assume a debtor-creditor relationship, one which does not impose a fiduciary duty unless a special relationship exists.¹³⁶ Here, the special relationship involved long-standing trust and confidence and the widow's reliance on the bank.¹³⁷ The court held that the vice-president "had an obligation to inform [plaintiff] fully as to his involvement in the ranch purchase and to do nothing which would place [plaintiff] at a disadvantage."¹³⁸ The court reasoned that "any breach of duty" means a fiduciary duty, which the vice-president breached through his failure to reveal his involvement in the purchase. Because the vice-president breached this duty, the plaintiff was entitled to rescission of the contract.

Morse and *Deist* were soon followed by other opinions holding that actionable constructive fraud requires a fiduciary duty. *Rowland v. Kleis*¹³⁹ followed *Morse*. In *Rowland*, the plaintiff inhabited a cabin situated on an acquaintance's mountain property.¹⁴⁰ Kleis, the acquaintance, offered the use of the cabin to Rowland as long as he maintained and inspected the property.¹⁴¹ The parties had a disagreement and agreed that Rowland would vacate the property after a certain date.¹⁴² Rowland later sued on numerous grounds, including negligent misrepresentation, which encompassed constructive fraud.¹⁴³ The lower court granted summary judgment for the defendant on the negligent misrepresentation claim.

The court held that the plaintiff's constructive fraud claim failed for lack of a fiduciary duty.¹⁴⁴ The court acknowledged that the plaintiff used the statutory language in his claim.¹⁴⁵ The court,

134. *Id.* at 215, 678 P.2d at 192.

135. *Id.* at 217-20, 678 P.2d at 193-95.

136. *Id.* at 216, 678 P.2d at 193.

137. Interestingly, although the bank vice-president did not act as a financial advisor or negotiator, the court extended fiduciary duty to him through his association with the bank.

138. *Deist*, 208 Mont. at 220, 678 P.2d at 195.

139. 223 Mont. 360, 726 P.2d 310 (1986).

140. *Id.* at 362, 726 P.2d at 312.

141. *Id.* at 363, 726 P.2d at 312.

142. *Id.* at 364, 726 P.2d at 313.

143. *Id.* at 367, 726 P.2d at 315.

144. *Id.* at 369, 726 P.2d at 316.

145. *Id.*

however, proceeded directly to *Morse* without exploring the possible breadth of the "any breach of duty" clause. Nor did the court grant that *Morse* involved an attorney-client relationship rather than the hybrid landlord-tenant and employer-employee relationship present in *Rowland*. Rather, the court ended its brief treatment of the constructive fraud issue by observing "nothing in the record [shows] a fiduciary relationship. Instead, [the litigants] were dealing with each other at arm's length."¹⁴⁶

The court remained tethered to its fiduciary duty requirement in *Pipinich v. Battershell*.¹⁴⁷ The court correctly found no duty to disclose, but still searched for a fiduciary relationship despite the clear wording of the constructive fraud statute.

Later, the court collapsed the two subdivisions of the statute into one and injected the fiduciary issue in *Bottrell v. American Bank*.¹⁴⁸ In *Bottrell*, the court offered this imprecise gloss on the plainly written statute: "Generally, an act or omission of a fiduciary or one in a confidential relationship is necessary to constitute constructive fraud."¹⁴⁹

If the *Morse* progeny seem to treat a developing doctrine in a cursory, imprecise manner, then the cases following *Mends* offer greater hope to the practitioner. Some of the confusion may have resulted from a lack of recent, substantive law in Montana on constructive fraud. The court has not borrowed much constructive fraud authority from other jurisdictions. Moreover, to its credit, the court may have adhered to the fiduciary duty requirement set forth in *Morse* in deference to *stare decisis*.

Mends and its progeny are more closely reasoned opinions. Unlike the *Morse* cases, the cases that follow *Mends* collect the pertinent authorities. The *Mends* cases hew to the statute and do not reflexively apply inappropriate precedent. These cases focus straightforwardly on the failure to disclose material flaws or other significant facts.

IV. RECOMMENDED APPROACHES

A. *The Practitioner*

Given these mixed signals, the practitioner must be wary of omitting a fiduciary duty theory under a constructive fraud claim

146. *Id.* The court's characterization of an "arm's length" exchange does not square with the fact that Kleis built the cabin for Rowland and occasionally stayed with him there.

147. 232 Mont. 507, 759 P.2d 148 (1988).

148. 237 Mont. 1, 773 P.2d 694 (1989).

149. *Id.* at 20, 773 P.2d at 706.

where a fiduciary duty clearly exists.¹⁵⁰ The advisable strategy is to use the fiduciary duty theory where the court recognizes it. Otherwise, practitioners must proceed with caution under a theory of special circumstances.

The court clearly will affirm a finding of constructive fraud under special circumstances, absent a fiduciary relationship. The lawyer must realize, however, that the court has recognized few contexts in the past decade where special circumstances supported a finding of constructive fraud absent a fiduciary duty.¹⁵¹

B. The Supreme Court

The court should adopt a consistent approach to constructive fraud. The lesson of the *Mends* cases is that the plaintiff who makes a major purchase pursuant to a fraudulently induced contract needs a claim to stay in court. Constructive fraud, as delimited by the statute, affords this remedy. Erecting the added barrier of fiduciary duty simply thwarts claims the statute should instead protect. The court, therefore, should adhere strictly to the statute as written.

V. COUNSELLING AND NEGOTIATION

In negotiating sales, counsel must recall (or remind clients acting as negotiators without counsel) that constructive fraud does not require dishonesty of purpose or intent.¹⁵² The lesson from *Moschelle*, *Mends* and *McGregor* is that, in negotiating, the seller must avoid misrepresentation,¹⁵³ must avoid creating false impressions regarding serious flaws,¹⁵⁴ and should refrain from a pattern of concealment regarding property.¹⁵⁵ These rules particularly apply where the seller knows of material flaws.¹⁵⁶ The seller must be careful not to create the perception of gaining advantage through

150. See *Purcell v. Automatic Gas Distrib., Inc.*, 207 Mont. 223, 673 P.2d 1246 (1983); *Morse v. Espeland*, 215 Mont. 148, 696 P.2d 428 (1985).

151. *Drilcon, Inc. v. Roil Energy Corp.*, 230 Mont. 166, 749 P.2d 1058 (1988); *McJunkin v. Kaufman & Broad Home Sys., Inc.*, 229 Mont. 432, 748 P.2d 910 (1987); *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981).

152. *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155, 158 (1980). See also 37 C.J.S. *Fraud* §2 (1943).

153. *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981). See also Annotation, *False Representations As To Income, Profits, or Productivity of Property As Fraud*, 27 A.L.R.2d 14 (1953).

154. *Moschelle v. Hulse*, 190 Mont. 532, 622 P.2d 155 (1980).

155. *Id.*

156. *Poulsen v. Treasure State Indus., Inc.*, 192 Mont. 69, 626 P.2d 822 (1981).

awareness of the buyer's apparent naivete.¹⁵⁷

Generally, the court seems to promote the exchange of accurate, pertinent business records. The court weighs refusal to provide business records¹⁵⁸ and failure to provide faithful financial statements.¹⁵⁹ Nonetheless, a bank has no duty to disclose an "Action Plan" calling for the liquidation of a struggling business if the operators are aware of losses and address cutting costs with the bank.¹⁶⁰ Counsel should advise clients to keep accurate records that truthfully reveal income and expenses, and to provide the records to serious potential buyers. Income projections, if provided during negotiations, should accurately reflect past performance of a business.¹⁶¹ Practitioners should also advise clients to avoid the appearance of a "runaround" and to refrain from making vain promises.¹⁶²

Counsel should keep abreast of the court's rulings on fiduciary duty, and whom it impacts—particularly bank clients.¹⁶³ Each case involving creditor and debtor should be carefully studied for indications of a fiduciary relationship. If the bank acts in an advisory capacity and has a lengthy course of dealing with the debtor, a fiduciary duty may be created.¹⁶⁴ In the constructive fraud context, the court has yet to particularize fiduciary relationships.

VI. LITIGATING THE CONSTRUCTIVE FRAUD CLAIM

A. Pleading

1. Venue

Plaintiffs with a constructive fraud claim may sue on the con-

157. *McGregor v. Mommer*, 220 Mont. 98, 101, 714 P.2d 536, 538 (1986).

158. *Moschelle*, 190 Mont. at 540, 622 P.2d at 160-61.

159. *Purcell v. Automatic Gas Distrib., Inc.*, 207 Mont. 223, 673 P.2d 1246 (1983).

160. *Coles Dep't Store v. First Bank (N.A.)-Billings*, 240 Mont. 226, 231, 783 P.2d 932, 935 (1989).

161. *See Amundson v. Wortman*, 238 Mont. 207, 777 P.2d 315 (1989).

162. *See Drilcon, Inc. v. Roil Energy Corp.*, 230 Mont. 166, 749 P.2d 1058 (1988).

163. *See Annotation, Existence of Fiduciary Relationship Between Bank and Depositor or Customer So As To Impose Special Duty of Disclosure Upon Bank*, 70 A.L.R.3d 1344 (1976).

164. *Simmons v. Jenkins*, 230 Mont. 429, 433, 750 P.2d 1067, 1070 (1988). However, where the debtor has advanced management and business degrees, lengthy management experience, and the bank has no financial management role, the bank does not breach a fiduciary duty to the creditor. *See Coles Dep't Store v. First Bank (N.A.)-Billings*, 240 Mont. 226, 230-33, 783 P.2d 932, 934-36 (1989). The practitioner should also heed *Deist v. Wachholz*, wherein the court extended a fiduciary duty to a bank officer who did not act as a negotiator or advisor in a real property transaction. *See supra* notes 128-38 and accompanying text for a discussion of *Deist*.

tract to recover damages.¹⁶⁵ Venue for actions "upon contracts is either: (a) the county in which the defendants . . . reside at the commencement of the action; or (b) the county in which the contract was to be performed."¹⁶⁶ If the plaintiff seeks to quiet title to, or recover, fraudulently procured real property, the venue is "the county in which the real property, or any part thereof, affected by such action or actions is situated."¹⁶⁷ Where the plaintiff seeks equitable relief not involving title to real property or a contract, venue is the county of the defendant's residence.¹⁶⁸

2. Remedies and Defenses

The defrauded party may repudiate the contract by rescinding it, or "affirm the contract and sue for damages."¹⁶⁹ If rescinding, the plaintiff must offer "prompt notice and offer to restore the consideration."¹⁷⁰ The remedy of rescission does not preclude other appropriate equitable relief, such as reconveyance of property.¹⁷¹ Defense counsel must treat constructive fraud as an affirmative defense.¹⁷² A defendant shall use constructive fraud as a defense in a counterclaim if the fraud "arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction."¹⁷³

3. The Complaint

The plaintiff need not plead constructive fraud with specificity, unlike actual fraud.¹⁷⁴ Allegations of matters uniquely "within the knowledge of the defendant . . . may be made on information and belief."¹⁷⁵ In certain scenarios, the constructive fraud claim alone may keep the plaintiff in court.¹⁷⁶ Therefore, the plaintiff's counsel should plead constructive fraud whenever the claim ap-

165. Constructive fraud is a contract claim, which falls under Title 28 of the Montana Code Annotated.

166. MONT. CODE ANN. § 25-2-121(1)(a), (b) (1989).

167. MONT. CODE ANN. § 25-2-123(3) (1989).

168. MONT. CODE ANN. § 25-2-118(1) (1989).

169. 34 CAL. JUR. 3D *Fraud and Deceit* § 59 (1977). The plaintiff may demand relief in the alternative. The plaintiff cannot both rescind the contract and affirm it, claiming damages. *Id.* at § 63.

170. 1 B. WITKIN, SUMMARY OF CALIFORNIA LAW *Contracts* § 321 (8th ed. 1973).

171. 34 CAL. JUR. 3D *Fraud and Deceit* § 60 (1977).

172. MONT. R. CIV. P. 8(c).

173. MONT. R. CIV. P. 13(a).

174. *Eaton v. Morse*, 212 Mont. 233, 242, 687 P.2d 1004, 1009 (1984).

175. 34 CAL. JUR. 3D *Fraud and Deceit* § 70 (1977).

176. *Deist v. Wachholz*, 208 Mont. 207, 678 P.2d 188 (1984).

pears well grounded in fact. The statute of limitations for bringing such a claim is two years.¹⁷⁷ The complaint should, where possible, allege constructive fraud in detail and state unambiguously the relief sought. The complaint should demonstrate reasonable diligence in detecting facts supporting the constructive fraud.¹⁷⁸

B. Discovery

Depositions may be used early in the litigation to pin parties down to their respective versions of representations made and the condition of property conveyed. Interrogatories should be used to identify other defendants, inspectors, appraisers, and accountants and to determine the existence of pertinent documents.¹⁷⁹ Requests for production of documents and requests for admissions may be used in tandem to identify and obtain relevant contracts, prospectuses, and financial records.

C. Proof and Evidence

Clearly, the plaintiff must prove the "existence of any duty," or "any act or omission considered fraudulent by law."¹⁸⁰ The plaintiff thereby must show that he or she reposed trust in the defendant, who occupied a superior position and gained an advantage to the prejudice of the plaintiff. To this end, the plaintiff should place the relationship within an established fiduciary relationship¹⁸¹ or emphasize that special circumstances (e.g., suppression of evidence of a material flaw,¹⁸² knowledge of the plaintiff's guilelessness,¹⁸³ communication of false impressions to a party acting in detrimental reliance¹⁸⁴) exist. Prejudice may be demonstrated by competent evidence of loss of value of property, and cost of improvements.¹⁸⁵

On direct examination, the plaintiff alleging constructive fraud should establish the date of representations and execution of any written agreement, and should relate the substance of the defend-

177. *Tynes v. Bankers Life Co.*, 224 Mont. 350, 357, 730 P.2d 1115, 1120 (1986).

178. 34 CAL. JUR. 3d *Fraud and Deceit* § 71 (1977).

179. See 5A BENDER'S FORMS OF DISCOVERY, *Fraud*, Interrogatory 3.2 (1989).

180. *Wiberg v. 17 Bar, Inc.*, 241 Mont. 490, 496, 788 P.2d 292, 295 (1990). See also *Fleming v. Fleming Farms, Inc.*, 221 Mont. 237, 717 P.2d 1103 (1986) (constructive fraud claim fails for lack of an established duty).

181. See *supra* notes 17-22 and accompanying text.

182. *Russell v. Russell*, 152 Mont. 461, 452 P.2d 77 (1969).

183. *McGregor v. Mommer*, 220 Mont. 98, 714 P.2d 536 (1986).

184. *Drilcon, Inc. v. Roil Energy Corp.*, 230 Mont. 166, 749 P.2d 1058 (1988).

185. 34 CAL. JUR. 3d *Fraud and Deceit* § 84 (1977).

ant's misrepresentations.¹⁸⁶ The plaintiff should state his or her reliance and describe the subsequent damages.¹⁸⁷ Direct examination should also elicit the price paid and any good faith inspection or determination of worth.¹⁸⁸

In Montana, the courts permit latitude for proof of fraud, and "every fact or circumstance from which a legal inference of fraud may be drawn is admissible."¹⁸⁹ Frequently, fraud cannot be proved by direct evidence.¹⁹⁰ Fraud may be proved by circumstantial evidence, therefore, the court allows the assembly of disconnected facts and circumstances.¹⁹¹ The fraud exception to the parol evidence rule¹⁹² encompasses constructive fraud.¹⁹³

Defense lawyers should beware of countering with assertions that the plaintiffs could, or did, inspect property or that defendants did not deliberately mislead.¹⁹⁴ Counsel should recall that the court has rejected the sellers' contention that they were not liable for constructive fraud because they did not deliberately mislead the purchasers of a home.¹⁹⁵ Similarly, the seller cannot defend by asserting that the plaintiffs had the opportunity to inspect a house with material, undisclosed defects that would require effort or a change in weather to discover.¹⁹⁶

Documents are critical in constructive fraud cases as the parties will have divergent views of the evidence, particularly verbal representations. Counsel should review all correspondence between the parties for misleading statements or omissions. Similarly, counsel should request from clients notes taken during inspections or negotiations.

VII. CONCLUSION

It is fruitless to attempt to reconcile the *Mends* cases and the contrary line of cases, the *Morse* cases. It would be misleading at best to force a synthesis of the past decade's several lines of thought on constructive fraud. A more sound approach to the con-

186. See 2 CYCLOPEDIA OF TRIAL PRACTICE § 523 (2d ed. 1970).

187. *Id.*

188. *Id.*

189. *Koch v. Rhodes*, 57 Mont. 447, 452, 188 P. 933, 935 (1920) (court allowed testimony by a third party as independent proof indicating that the seller of a ranch knew the falsity of the representations).

190. *Merchants' Nat'l Bank v. Greenhood*, 16 Mont. 395, 41 P. 250 (1895).

191. *Roman v. Albert*, 81 Mont. 393, 264 P. 115 (1928).

192. MONT. CODE ANN. § 28-2-905(2) (1989).

193. *Eaton v. Morse*, 212 Mont. 233, 242, 687 P.2d 1004, 1008 (1984).

194. See *Mends v. Dykstra*, 195 Mont. 440, 637 P.2d 502 (1981).

195. *Moschelle v. Hulse*, 190 Mont. 532, 537, 622 P.2d 155, 158 (1980).

196. *Mends*, 195 Mont. at 451-52, 637 P.2d at 508 (1981).

trary holdings is simply to realize that the court will find constructive fraud liability where a known fiduciary duty exists, but that a fiduciary duty is not always a requirement. This latter statement is true when special circumstances exist, such as a duty to refrain from creating false impressions (where reliance is a factor) or the duty to disclose material, hidden defects in property conveyances.

